Research Update:

Infrastrutture Wireless Italiane S.p.A. Assigned 'BB+' Rating; Outlook Stable

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Rating Action Overview

- Infrastrutture Wireless Italiane S.p.A. (INWIT) operates in the credit-supportive tower industry, with very high barriers and protective all-or-nothing, CPI-indexed long-term contracts.
- It has a very strong, distant leading domestic position in Italy, and will generate robust and resilient cash flows.
- We also anticipate steady growth in revenues and EBITDA on the back of ongoing 5G deployment and 4G densification investments.
- The company has high, industry-typical customer concentration, and high leverage, but we expect its metrics to gain increasing headroom within the rating guidelines thanks to EBITDA growth.
- We are assigning our 'BB+' long-term issuer credit rating to INWIT.
- The stable outlook reflects our view that management will smoothly execute the merger of Telecom Italia Group's (TIM's) and Vodafone's tower portfolios, planned synergies, and the 5G deployment; and leverage INWIT's very strong market position to sustain an S&P Global Ratings-adjusted leverage below 6x.

Rating Action Rationale

The tower industry enjoys very supportive credit characteristics. The wireless tower industry's low risk profile reflects the sector's low volatility and cyclicality, and the high predictability of cash flows, given its critical infrastructure nature. This is further supported by typically long-term contracts between tower companies and telecommunications carrier customers; very high barriers to entry, due in particular to permitting and land sourcing constraints; and the very difficult replication of established networks. In addition, the industry enjoys favorable long-term growth prospects from increasing demand for mobile data and video and continued investment by telecom carriers in wireless networks, including for the 5G technology deployment. Frequencies acquired by mobile network operators (MNOs) recently were tied to 5G coverage obligations, which make 5G-related growth opportunities for INWIT more certain.

The company has a very strong market position in Italy. It boasts a very strong position of in Italy, capturing about half of the Italian tower market through a nationwide dense network of 22,000 sites hosting about 39,000 points of presence, and ranks distantly ahead of the nos. 2 and 3 tower operators (Cellnex and WindTre). The network overlap with competition is limited, which strengthens INWIT's pricing power. The company does not compete at the national level against Italian incumbents TIM and Vodafone, because its network would comprise the entirety of the latter two's towers. This translates into a domestic market position that is significantly stronger than that of European peers such as TDF in France and Cellnex in Spain, in our view. INWIT's domestic position is more comparable with that of its smaller-scale Mexican peer Operadora de Sites Mexicanos. Moreover, the company's nearest competitors are relatively distant, which further strengthens is position and should support growth on the back of 4G densification and 5G build-up, further underpinned by the preferred supplier agreement with TIM and Vodafone.

INWIT operates a high quality network under protective long-term contracts. The high quality of the company's site network stems from its favorable locations, reflecting the historically first movers' advantage of TIM's and Vodafone's networks, as well as a meaningful degree of its tower backhaul being equipped with fiber, a more powerful technology than traditional airwaves to connect the radio sites to the clients' local exchanges. In addition, INWIT operates under extremely protective, eight-year, indefinitely renewable, all or nothing, CPI-indexed (with 0% floor) contracts signed with TIM and Vodafone, providing high revenue visibility.

INWIT's heavy customer concentration, which is typical for the industry, is not a ratings constraint, given the critical nature of its services and the credit standing of customers. The company's revenues are heavily concentrated on TIM and Vodafone, which together account for about 90% of total revenue. In this regard, INWIT is significantly less diversified than Cellnex, both in terms of countries and end-customers. We don't see a mechanical link between the company's credit quality and that of its customers, given the infrastructure and critical nature of its services for mobile operators. Still, any increasing divergence between INWIT's credit quality and that of either main client could ultimately become a more material constraint on the company's business risk profile and the overall rating.

INWIT has a strong operating efficiency track record and meaningful synergies likely from the merger of TIM's and Vodafone's networks. Management's track record is solid, reflected in steady increases in colocation and revenues per site, as well as ongoing reduction in ground lease costs achieved since 2015. Significant potential synergies exist, ranging from ground leases, optimized site portfolio, and increased colocation on existing sites. This stems from INWIT's post-merger stronger local position, as well as the passive and active network sharing between TIM and Vodafone, that will free up space for third parties; and the antitrust remedies requiring additional site opening to third parties.

INWIT has higher margins and a stronger domestic position than most of its rated peers. These are in line with those of Operadora de Sites Mexicanos (BB+/Stable/--). The company has also significantly greater scale than France-based Tivana France Holdings (TDF; BBB-/Stable/--), while Cellnex (BB+/Stable/--) has a larger scale and broader markets and clients diversity than INWIT. Overall, we view both INWIT and Cellnex in the high end of the strong business risk profile category; TDF's business profile is weaker, but its significantly lower debt leverage translates into a higher rating. While the European and Mexican players' business risk profiles are in the strong category, U.S. peers' business risk profiles are in the higher excellent category, because they enjoy a much larger scale across the country and operate in the very mature and consolidated U.S.

market.

Outlook

The stable outlook reflects our view that management will smoothly execute the merger of TIM's and Vodafone's tower portfolios, and leverage the extended network sharing opportunities, as well as INWIT's very strong market position and favorable MNO market context, to generate new revenues on 4G sites densification and the 5G rollout kickoff. We also anticipate continuation of the solid operating efficiency track record, and the successful execution of cost synergies allowed by the merged network optimization.

The stable outlook also reflects our forecasts that S&P Global Ratings-adjusted leverage, funds from operations (FFO)-to-debt and free operating cash flow (FOCF)-to-debt ratios will sustainably remain below 6x, and above 12% and 7%, respectively.

Downside scenario

We could lower our rating on INWIT should we see:

- Any setbacks in the merger or implementation of development plans; or
- S&P Global Ratings-adjusted debt to EBITDA above 6x, or S&P Global Ratings-adjusted FFO to debt or FOCF to debt to below 12% and 7%, respectively, due to operational setbacks or a more aggressive financial policy than foreseen.

Upside scenario

Ratings upside would exist should the following happen:

- Swift progress in merger execution and management's development and refinancing plans;
- S&P Global Ratings-adjusted leverage, FFO-to-debt, and FOCF-to-debt ratios improved to less than 5x, above 15%, and 10% respectively;
- We are comfortable these levels, which could be reached by 2022, are sustainable and that management is willing to sustain leverage at below 5x.

At this stage, we understand that management target a leverage of less than 6x, so we would not expect leverage of lower than 5x to be sustained.

Company Description

INWIT is the largest independent cellphone tower company (towerco) in Italy and the second-largest independent towerco in Europe, with more than 22,000 towers.

Our Base-Case Scenario

Assumptions

- A severe recession this year due to the economic fallout from the coronavirus pandemic. We now expect GDP to fall about 9.9% in Italy in 2020. Still, we expect towercos like INWIT to demonstrate strong resilience through the COVID-19 outbreak because the sector's low cyclicality and utility-like characteristics. We expect GDP to rebound to about 6.4% growth in Italy in 2021
- Revenues of €700 million-€800 million in 2020, pro forma 12 months' consolidation of Vodafone's towers, up 2% over pro forma 2019
- Revenue growth accelerating from next year, with revenues up 8% in 2021 and 10% in 2022, driven in particular by additional points of presence rented to TIM and Vodafone in the existing network and a rapid take off of small cells to expand the 5G indoor coverage
- Reported EBITDA margin of about 90% before leases, with absolute EBITDA rising along with revenue
- Heavy growth-oriented capital expenditure of about 20% of sales over 2020-2022, including hefty spending on land acquisitions and small cell deployments
- Maintenance capital expenditure of about 1% of sales
- Cost of financial debt of about 1.9% all-in over 2020-2022
- Ordinary dividend payments of about €127 million in 2020
- No acquisitions or share buyback

Key metrics

Year ended Dec. 31	2020F	2021F	2022F
EBITDA margin (%)	89.7	90.4	90.9
FFO to debt (%)	12.3	13.7	15.4
FOCF to debt (%)	8.5	9.0	10.5
Debt/EBITDA (x)	5.9	5.4	4.8

A--Actual. F--Forecast. FFO--Funds from operations. FOCF—Free operating cash flows. Figures are adjusted.

Liquidity

We assess INWIT's liquidity as adequate based on our expectation that liquidity sources will exceed uses 1.2x in the 12 months started March 31, 2020. In addition, we think INWIT has sound relationships with its banks. Access to capital markets is yet untested, but we foresee smooth refinancing of its €1.5 billion bridge loan within two years given the resilient business risk profile.

As of March 31, 2020, pro forma the merger closure and €570 million exceptional dividends, we estimate that principal liquidity sources over the ensuing 12 months include:

- €300 million of undrawn availability under its €500 million, five-year revolver, which do not contain material adverse clauses
- S&P Global Ratings' forecast of pro forma FFO of about €300 million after leases

For the same period, we estimate that principal liquidity uses include:

- S&P Global Ratings' forecast of capital expenditures of €100-200 million, net of IRUs received for backhauling deployments
- Ordinary dividend payments of about €127 million

Covenants

INWIT's debt package comprises a maintenance covenant tested every semester.

Compliance expectations

We expect adequate headroom under the covenant.

Ratings Score Snapshot

Issuer Credit Rating: BB+/Stable/--

Business risk: Strong

- Country risk: Moderately high
- Industry risk: Intermediate
- Competitive position: Strong

Financial risk: Highly leveraged

- Cash flow/Leverage: Highly leveraged

Anchor: bb

Modifiers:

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Positive (+1 notch)

Stand-alone credit profile: bb+

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014

- Criteria | Corporates | Industrials: Key Credit Factors For The Telecommunications And Cable Industry, June 22, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

New Rating;

Infrastrutture Wireless Italiane S.p.A.	
Issuer Credit Rating	BB+/Stable/--